

AMENDED IN SENATE APRIL 18, 2006

AMENDED IN SENATE MARCH 27, 2006

SENATE BILL

No. 1452

Introduced by Senator Speier

February 23, 2006

An act to amend Sections 1236, 1237, and 8546.5 of, to add Section 8546.2 to, to add Article 4 (commencing with Section 8548.7) to Chapter 6.5 of Division 1 of Title 2 of, and to add Part 3.5 (commencing with Section 13885) to Division 3 of Title 2 of, the Government Code, and to amend Sections 11751.5 and 11873 of the Insurance Code, relating to state audits.

LEGISLATIVE COUNSEL'S DIGEST

SB 1452, as amended, Speier. State audits.

(1) Existing law requires that the Controller, the Director of Finance, and the respective staffs of all state agencies that have their own internal auditors or that conduct internal audits or internal audit activities, and all city, county, city and county, and district employees that conduct internal audits or internal audit activities of those respective agencies, utilize the general and specified standards of internal auditing specified in a publication of the Institute of Internal Audits.

This bill instead would require these entities to conduct their work under the general and specified standards prescribed by the Institute of Internal Auditors or the Government Auditing Standards issued by the Comptroller General of the United States, as appropriate, and except as specified.

(2) Existing law sets forth the duties and authority of the State Auditor generally in conducting audit activities on behalf of the state.

This bill would require the State Auditor to request that any state or local agency, or any publicly created entity, that is the subject of an audit conducted under these provisions to provide updates on its progress in implementing the recommendations made by the State Auditor, at intervals prescribed by the State Auditor. It would require state agencies to provide these updates to the State Auditor.

This bill would enact the Omnibus Audit Accountability Act of 2006, to require the State Auditor to, by January 15th of each year, report to specified entities with respect to each state agency audit recommendation it has made that is more than one year old and that has not been implemented by the affected agency. It would require any state agency that is notified by the State Auditor that it has not implemented a recommendation made pursuant to this chapter more than one year prior, to provide specified information in that regard.

(3) Existing law authorizes the State Auditor to establish a high-risk government agency audit program for the purpose of identifying, auditing, and issuing reports on any agency of the state, that the State Auditor identifies as being at high risk for the potential of waste, fraud, abuse, and mismanagement or that has major challenges associated with its economy, efficiency, or effectiveness, subject to specified criteria.

This bill instead would require the State Auditor to establish this program.

(4) Existing law requires all state and local agencies with an aggregate spending of \$50,000,000 or more annually to consider establishing an ongoing internal audit function.

This bill instead would apply this provision to local agencies only.

The bill would require all state agencies with an aggregate spending of \$100,000,000 or more annually, as specified, to establish an ongoing internal audit function, subject to specified criteria, or enter into an interagency agreement with the Department of Finance that provides for an audit function. It would require any governing body that oversees a state agency with that aggregate spending amount to establish an audit committee, subject to specified criteria. It would set forth the requirements for reporting audit findings and recommendations by chief internal auditors, and specifically provide that an individual reporting certain information under these provisions is protected under provisions of law protecting state employees from retaliation for reporting waste, fraud, or abuse. It would further require the State Auditor to annually select not less than 2 state agencies and

conduct a performance audit of the internal audit organizations within the selected state agencies to determine whether the audit organizations are meeting the requirements of these provisions.

(5) Existing law requires the Insurance Commissioner to designate a licensed rating organization as his or her statistical agent to gather and compile insurer experience statistics for specified purposes.

This bill would specify that the designated statistical agent is a publicly created entity for purposes of audits by the State Auditor.

(6) Existing law exempts the State Compensation Insurance Fund from certain provisions of law applying to state agencies, with specified exceptions.

This bill would specify that the fund is subject to the provisions of law governing audits by the State Auditor.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. Section 1236 of the Government Code is
2 amended to read:

3 1236. (a) All city, county, city and county, and district
4 employees that conduct internal audits or that conduct internal
5 audit activities of those respective agencies; shall conduct their
6 work under the general and specified standards prescribed by the
7 Institute of Internal Auditors or the Government Auditing
8 Standards issued by the Comptroller General of the United
9 States, as appropriate.

10 (b) Nothing in this section is intended to limit the rights or
11 obligations of internal auditors to conduct internal audits and
12 audit activities in accordance with other laws and regulations that
13 may apply to a particular entity.

14 SEC. 2. Section 1237 of the Government Code is amended to
15 read:

16 1237. All local agencies with an aggregate spending of fifty
17 million dollars (\$50,000,000) or more annually shall consider
18 establishing an ongoing internal audit function.

19 SEC. 3. Section 8546.2 is added to the Government Code, to
20 read:

21 8546.2. (a) The State Auditor shall request that any state
22 agency, as defined in Section 11000, whether created by the

1 California Constitution or otherwise, any local governmental
2 agency, including any city, county, city and county, school, or
3 special district, or any publicly created entity, that is the subject
4 of an audit conducted pursuant to this chapter provide updates on
5 its progress in implementing the recommendations made by the
6 State Auditor, at intervals prescribed by the State Auditor.

7 (b) Any state agency described in subdivision (a) shall provide
8 the State Auditor, in the form prescribed by the State Auditor,
9 with updates on implementation of recommendations as
10 described in subdivision (a).

11 SEC. 4. Section 8546.5 of the Government Code is amended
12 to read:

13 8546.5. (a) The State Auditor shall establish a high-risk
14 government agency audit program for the purpose of identifying,
15 auditing, and issuing reports on any agency of the state, whether
16 created by the California Constitution or otherwise, that the State
17 Auditor identifies as being at high risk for the potential of waste,
18 fraud, abuse, and mismanagement or that has major challenges
19 associated with its economy, efficiency, or effectiveness.

20 (b) In addition to identifying an agency as high risk on the
21 basis of weaknesses identified in audit and investigative reports
22 produced by the bureau, the State Auditor may consult with the
23 Legislative Analyst, the Milton Marks “Little Hoover”
24 Commission on California State Government Organization and
25 Economy, the Office of Inspector General within the Department
26 of Corrections, the Department of Finance, and other state
27 agencies that have oversight responsibilities over any other
28 agency of the state, in identifying state agencies that are at high
29 risk.

30 (c) The State Auditor shall notify the Joint Legislative Audit
31 Committee whenever it identifies a state agency as at high risk.

32 (d) The State Auditor may issue audit reports with
33 recommendations for improvement in state agencies identified as
34 at high risk not less than once every two years.

35 (e) The State Auditor may require state agencies identified as
36 high risk to periodically report to the auditor regarding the status
37 of recommendations for improvement made by the State Auditor
38 or other state oversight agencies.

1 SEC. 5. Article 4 (commencing with Section 8548.7) is added
2 to Chapter 6.5 of Division 1 of Title 2 of the Government Code,
3 to read:

4
5 Article 4. Omnibus Audit Accountability Act of 2006
6

7 8548.7. This article shall be known and may be cited as the
8 Omnibus Audit Accountability Act of 2006.

9 8548.9. (a) The State Auditor shall, by January 15th of each
10 year, report to the Joint Legislative Budget Committee, the Joint
11 Legislative Audit Committee, and the Department of Finance
12 with respect to each state agency audit recommendation it has
13 made that is more than one year old and that has not been
14 implemented by the affected agency.

15 (b) The report shall clearly identify the state agency audited,
16 the audit that contained the recommendation, a brief description
17 of the recommendation, the date it was issued, and the most
18 recent explanation provided by the agency to the State Auditor
19 on the status of the recommendation.

20 (c) Any state agency that is notified by the State Auditor that it
21 has not implemented a recommendation made pursuant to this
22 chapter more than one year prior, shall do either of the following:

23 (1) Provide a written report to the State Auditor, the respective
24 policy committees and budget subcommittees of the Assembly
25 and Senate with oversight of the agency, and the Department of
26 Finance, explaining why the audit recommendation has not been
27 implemented.

28 (2) Notify all entities described in subdivision (a) that it will
29 begin implementing the audit recommendation within 90 days of
30 the notification by the State Auditor, and include the estimated
31 date of implementation.

32 SEC. 6. Part 3.5 (commencing with Section 13885) is added
33 to Division 3 of Title 2 of the Government Code, to read:

34
35 PART 3.5. INTERNAL AUDITS
36

37 13885. The Legislature finds and declares as follows:

38 (a) Recent corporate scandals and federal legislation, such as
39 the Sarbanes-Oxley Act of 2002 (~~Pub.~~ (P.L. No. 107-204), focus

1 attention on the importance of internal audit activity to public
2 accountability and governance.

3 (b) Ensuring the independence of internal auditors of state
4 agencies and that their findings are reported to the appropriate
5 levels of government is critical to safeguarding public funds and
6 the public trust.

7 13886. (a) (1) All state agencies with an aggregate spending
8 of one hundred million dollars ~~(\$100,000,00)~~ (\$100,000,000) or
9 more annually shall either establish an ongoing internal audit
10 function or enter into an interagency agreement with the
11 Department of Finance that provides for an audit function. The
12 funding threshold for compliance with this subdivision shall not
13 include any moneys subject to a single audit requirement
14 pursuant to federal regulations.

15 (2) For purposes of this chapter, “state agency” has the same
16 meaning as set forth in Section 11000, whether created by the
17 California Constitution or otherwise.

18 (b) Any governing body that oversees a state agency with the
19 aggregate spending described in subdivision (a) shall establish an
20 audit committee that generally meets the frameworks
21 recommended by the American Institute of Certified Public
22 Accountants, as set forth in the publication entitled “AICPA
23 Audit Committee Toolkit: Government Organizations.”

24 13886.5. (a) The Controller, the Director of Finance, and the
25 respective staffs thereof, and all state agencies that have their
26 own internal auditors or that conduct internal audits or internal
27 audit activities, shall conduct internal audit activity under the
28 general and specified standards of internal auditing prescribed by
29 the Institute of Internal Auditors or the Government Auditing
30 Standards issued by the Comptroller General of the United
31 States, as appropriate.

32 (b) Nothing in this ~~section~~ *article* is intended to limit the rights
33 or obligations of internal auditors to conduct internal audits and
34 audit activities in accordance with other laws and regulations that
35 may apply to a particular entity.

36 13887. (a) In order to achieve independence and objectivity
37 pursuant to Section 13886, for any state agency that does not
38 report to a governing body, the internal auditor operations shall
39 meet all of the following requirements:

1 (1) The chief internal auditor shall be accountable to the head
2 or deputy head of the state agency.

3 (2) The chief internal auditor shall report audit findings and
4 recommendations made under his or her jurisdiction to the head
5 or deputy head of the state agency and to the general counsel to
6 the state agency, if applicable.

7 (3) The operations shall be organizationally outside the staff or
8 line management function of the unit under audit.

9 (b) In order to achieve independence and objectivity as
10 required by the standards identified in Section 13886, for any
11 state agency that is overseen by a governing body, the internal
12 audit operations shall meet all of the following requirements:

13 (1) The chief internal auditor shall be accountable to the audit
14 committee of the governing body.

15 (2) The chief internal auditor shall report audit findings and
16 recommendations made under his or her jurisdiction to the audit
17 committee and the general counsel to the governing body.

18 (3) The operations shall be organizationally outside the staff or
19 line management function of the unit under audit.

20 13887.5. (a) When the chief internal auditor of a state agency
21 believes that senior management in the state agency has accepted
22 a level of residual risk that may be unacceptable to the
23 organization or that senior management has otherwise not taken
24 appropriate action in response to a finding or recommendation by
25 its internal auditors, the chief internal auditor shall discuss the
26 matter with senior management and the general counsel to the
27 state agency. If that decision regarding residual risk or the need
28 for appropriate action in response to an audit finding or
29 recommendation, or both, does not resolve the issue, the chief
30 internal auditor and general counsel shall jointly report the matter
31 to the next highest level of management as pertains to the state
32 agency, including, but not limited to, the chair of the governing
33 body overseeing the state agency, the agency secretary, the
34 Governor's office, or the appropriate constitutional officer.

35 (b) If the decision regarding residual risk or the need for
36 appropriate action in response to an audit finding or
37 recommendation that could have a significant impact on the
38 state's fiscal operations, the performance of a significant
39 government program, or the delivery of a significant government
40 service, or other similar significant or critical government

1 services, as determined by the chief internal auditor, is still not
2 resolved after making the disclosures required pursuant to
3 subdivision (a), the chief internal auditor shall report the matter
4 to the Joint Legislative Audit Committee and the State Auditor.
5 At the direction of the Joint Legislative Audit Committee, the
6 State Auditor shall investigate a disclosure made pursuant to
7 subdivision (b) and report the results of the investigation in
8 accordance with Chapter 6.5 (commencing with Section 8543) of
9 Division 1. The disclosure requirements of this subdivision shall
10 not apply to any chief internal auditor who reports and ~~make~~
11 *makes* disclosures to an audit committee, as described in
12 subdivision (b) of Section 13887.

13 (c) Any chief internal auditor who makes a disclosure pursuant
14 to this section shall receive all protection available under the
15 California Whistleblower Protection Act (Article 3 (commencing
16 with Section 8547) of Chapter 6.5 of Division 1).

17 13888. (a) If an internal auditor employed by a state agency
18 has a good faith belief that the agency management is interfering
19 with the internal auditor's or auditors' ability to comply with the
20 provisions of this part, that the internal auditor or auditors are
21 under pressure to modify or limit findings or recommendations,
22 or that senior management is not taking appropriate action in
23 response to an audit finding or recommendation, the internal
24 auditor may report the information supporting that good faith
25 belief to the State Auditor.

26 (b) The State Auditor may investigate any report made
27 pursuant to subdivision (a) and if the allegations are
28 substantiated, shall report his or her findings pursuant to Chapter
29 6.5 (commencing with Section 8545) of Division 1.

30 (c) Any internal auditor making a report pursuant to this
31 section shall receive all protection available under the California
32 Whistleblower Protection Act (Article 3 (commencing with
33 Section 8547) of Chapter 6.5 of Division 1).

34 13888.5. In order to determine that internal audit
35 organizations have the controls in place to ensure that they are
36 free to independently conduct audit work, and that state agencies
37 take appropriate action in response to the findings and
38 recommendations made by their internal auditors, the State
39 Auditor shall annually select not less ~~that~~ *than* two state agencies
40 and conduct a performance audit of the internal audit

1 organizations within the selected state agencies for that fiscal
2 year to determine whether the audit organizations are meeting the
3 requirements of this chapter.

4 SEC. 7. Section 11751.5 of the Insurance Code is amended to
5 read:

6 11751.5. The commissioner, after notice and hearing, may
7 promulgate reasonable rules and statistical plans, which may be
8 modified from time to time and which shall be used thereafter in
9 the recording and reporting by insurers of their loss and expense
10 experience in order that the experiences of all insurers may be
11 made available in such form and detail as may be necessary to
12 aid the commissioner in administering the provisions of Article 2
13 (commencing with Section 11730). The commissioner shall
14 designate a rating organization licensed under this article as his
15 or her statistical agent to gather and compile those experience
16 statistics and all licensed rating organizations shall report the
17 experience of their members to the designated rating
18 organization. The designated statistical agent is a publicly created
19 entity for purposes of Chapter 6.5 (commencing with Section
20 8543) of Division 1 of Title 2 of the Government Code. Subject
21 to reasonable rules approved by the commissioner, the designated
22 rating organization shall make the experience statistics, when
23 compiled, available to all licensed rating organizations and may
24 make a reasonable charge to other rating organizations for the
25 expense incurred by it in combining, tabulating, and compiling
26 the experience of all workers' compensation insurers.

27 SEC. 8. Section 11873 of the Insurance Code is amended to
28 read:

29 11873. (a) Except as provided by subdivision (b), the fund
30 shall not be subject to the provisions of the Government Code
31 made applicable to state agencies generally or collectively, unless
32 the section specifically names the fund as an agency to which the
33 provision applies.

34 (b) The fund shall be subject to the provisions of Chapter 10.3
35 (commencing with Section 3512) of Division 4 of Title 1 of, and
36 Chapter 6.5 (commencing with Section 8543) of Division 1 of
37 Title 2 of, the Government Code, and Division 5 (commencing
38 with Section 18000) of Title 2 of the Government Code, with the
39 exception of all of the following provisions of that division:

1 (1) Article 1 (commencing with Section 19820) and Article 2
2 (commencing with Section 19823) of Chapter 2 of Part 2.6 of
3 Division 5.

4 (2) Sections 19849.2, 19849.3, 19849.4, and 19849.5.

5 (3) Chapter 4.5 (commencing with Section 19993.1) of Part
6 2.6 of Division 5.

7 (c) Notwithstanding any provision of the Government Code or
8 any other provision of law, the positions funded by the State
9 Compensation Insurance Fund are exempt from any hiring
10 freezes and staff cutbacks otherwise required by law. This
11 subdivision is declaratory of existing law.